A Consumer's Guide to:

Life Insurance

What you should know about shopping for life insurance

Washington State
Office of the
Insurance Commissioner

www.insurance.wa.gov

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A consumer's guide to life insurance

You can obtain life insurance policies through agents or brokers, by mail, via the Internet, or through group plans offered by your employer or an association.

No matter how you buy your life insurance, you should only buy from a licensed company that offers policies approved in Washington state.

To protect you, the Office of the Insurance Commissioner (OIC) regulates all insurance transactions that take place in Washington state. To operate in our state, insurance companies must be licensed with our agency. Insurance companies must also file their policies with us.

In addition to our protections, state law created the Washington Life and Disability Guaranty Association. The association protects policyholders when insurance companies become unable to pay claims.

To find out if a company is licensed in our state, call our Insurance Consumer Hotline at 1-800-562-6900. You can also look the company up on the Web at http://www.insurance.wa.gov. Go to "For Consumers" and click on "Authorized Companies."

Deciding how much insurance to buy

You should decide how much life insurance you need. You need to look carefully at your individual circumstances. The real value of life insurance is to protect your loved ones after your death. Before you buy, ask yourself:

- What costs and hardships will my family have to deal with after I am gone?
- How will the loss of my salary affect my family?

These questions require careful thought and perhaps a candid talk with your beneficiaries.

Insurance shopping tips

First, set the goals you want. Then shop around. The cost of insurance varies from company to company—as do their services, standards, and policies.

Research the policy carefully to make sure it meets your needs. Once you decide to buy life insurance, don't delay! Make the purchase. Your beneficiaries will not benefit unless you buy a policy. Also, if you wait, you could develop a health problem, which could cause the rates to go up, or the company could reject your application.

The company must provide you with a buyer's guide and a policy summary before they give you the policy. If you do not receive these two items, ask for them.

The "free look" rule

- When you receive your new policy, read it carefully.
- Every new life insurance policy issued in Washington state comes with a 10-day "free look" period.
- If you are not satisfied for any reason, you may return the new policy within 10 days after you receive it.
- Mail it to the company's home office or give it back to the agent who sold it to you.
- Be sure to get a dated receipt from the post office or the agent.
- The company must return your premium within 30 days from the date you returned the policy. If they keep your money longer, legally they are responsible for a 10 percent penalty—payable to you.

How to buy life insurance

Mail order

A few insurance companies sell through the mail. You mail a completed application directly to the company. The company usually does not have an agent in your hometown.

The Internet

A growing number of insurance companies are expanding their marketing and are starting to sell policies on the Web. All state laws and regulations regarding selling insurance apply to the Internet and insurance-based Web sites. Do your research and make sure the company is authorized to do business in Washington state. If you have questions, call our Insurance Consumer Hotline at **1-800-562-6900**.

Agents and brokers

Most people buy life insurance through an agent or broker. Agents and brokers operate differently.

> **Agents** represent one or more companies. The agent's job, which is commission based, is to sell you the policies of the company he or she represents.
>
> **Brokers** represent and work for you. Typically, you describe to the broker the type of coverage you want and the amount you want to spend. The broker surveys the market and brings back options for you to review. Brokers also receive a commission on the sales they arrange.

Choose your agent or broker carefully. It is wise to select someone who is an established business person in your community. You may wish to ask, "What makes you feel you are qualified to talk to me about my financial security?" Reliable salespeople should not mind verifying their credentials or listing their qualifications.

If you have concerns about an insurance provider or a sales offer, contact our Insurance Consumer Hotline at **1-800-562-6900**.

What to do if a company turns you down

If a company turns you down for a policy, try another company. Companies use different methods and factors to decide whether or not to insure you. For example if you have high blood pressure that you control with medication, one company might reject you while another company may accept you.

If you have a medical problem, it's a good idea to talk it over with your doctor. Treatments may improve your condition enough to meet company standards, or the company may qualify you as a special risk at an adjusted premium. If the company uses your medical information to arrive at its rating, it must share that information with your doctor at your request.

You might also want to check on group life insurance. Some group plans do not require medical exams or health histories.

Insurance companies are part of the free enterprise system and can – within certain limits – select those individuals they want to insure. However, they are not free to turn down coverage without a valid reason. Under Washington state law, insurers cannot refuse insurance to anyone based on:

- sex
- marital status
- race
- creed
- color
- national origin

It's also against the law to deny coverage to domestic violence victims. And it's illegal to refuse people with a sensory, mental, or physical problem – except when the company can prove statistically that someone is more likely to file a claim.

If you feel an insurance company is treating you unfairly, you can file a complaint with our agency by calling **1-800-562-6900**. We will look into the issue on your behalf.

What you should know about your insurance company

Different companies offer different products. Some companies work with agents you can find in the phone book. Other companies prefer to deal directly with you.

One other key item you should think about before you buy is the financial security of the insurance company. As with most businesses, the security of a company depends on how it is managed, supervised, and controlled.

Rating your insurance company

One way to find out about your insurance company is to check its security rating. Several independent rating organizations monitor the financial strength of insurance companies. They also offer free rating information by phone and on the Web. These rating organizations include:

- A.M. Best Co., publisher of "Best Insurance Reports"
  908-439-2200, www.ambest.com
- Moody's Investor Service, Inc.
  212-553-0377, www.moodys.com
- Standard & Poor's
  1-800-523-4534, www.standardandpoor.com
- Duff & Phelps
  312-368-3100, www.dcrco.com
- Weiss Research
  1-800-289-9222, www.weissratings.com

Be aware that each organization uses its own criteria to determine financial ratings. Even though all use some form of "A," "B," or "C" grading system, what is "AAA" for one might be "A+" or "A-" for another.

What you should know about life insurance premiums

Premiums are the dollar amount you pay into a life insurance policy. Depending on your arrangement with the insurance company, you can pay premiums on a monthly basis or less often. All policies must contain a 31-day grace period for late payments. This means if you are late paying your premium, your policy still stays in effect for 31 days, until you pay your premium.

For group life insurance, employers can deduct your premiums with your permission from your paycheck.

Insurers base your life insurance premium on several factors:

- Age
- Health problems
- Occupation
- Hobbies
- Habits
- Other circumstances that may reduce your life span, such as a bad driving record or participating in dangerous activities
- Expenses the company expects to pay regarding your coverage, such as sales charges, and underwriting and administration costs
- Interest the company expects to earn from investing your premiums

What you should know about life insurance policies

A life insurance policy is a legal contract between you and the insurance company. This contract spells out:

- The rights and duties of you and the company
- How much and how often you pay
- The benefits you are entitled to receive
- The circumstances under which the policy will pay benefits

The best insurance policy is the one that best fits your needs. However, what is best for you right now, may not suit your situation 10 years from now. This means you should review your coverage regularly, even on an annual basis to make sure your coverage is current.

Term life and cash value life insurance

Term and cash value insurance are the two basic types of life insurance that companies offer in various forms.

Term insurance

Term insurance gets its name because it protects you for a specific "term"—usually a year or a limited number of years. You have to pay more for it as you get older because your risk of dying increases with age. Term insurance does not have a cash value and you cannot cash it in. Once the term ends, the policy no longer covers you. If the policy is renewable, you may buy it for another term at a rate guaranteed in the policy, without providing health information and some other proof of insurability, such as a driving record. However, the renewed policy will usually cost more. Over time, it may be too costly to renew.

Term insurance is well suited to fill a temporary need for increased insurance. If you leave one job for another, you may not have group life insurance coverage through your employer for a short time. Term insurance offers an easy purchase to bridge such a gap. It is also provides you with an option to quickly supplement an existing whole life policy with additional coverage.

Cash value life

For this type of insurance, you pay higher premiums at the beginning of the policy. The company uses part of your premium to set up an account under your policy with a cash value that you may use in a variety of ways. For example:

- You may borrow against a policy's cash value by taking out a loan. If you don't pay back the loan and the interest on it, the company will subtract the amount you owe from the benefits when you die. If you cancel the policy, the company will also subtract the loan balance from the cash value you receive
- You can use the cash value to pay an overdue premium on the policy
- You can use the cash value to increase your income in retirement or to provide for other financial needs. However, to build up this cash value, you must pay higher premiums in the early years of the policy

Whole life, universal life, and variable life

These are all considered types of cash value insurance. For whole life and universal life, the life insurance company invests your cash value as a general asset of the company. The interest the company credits to your cash value is based on its earnings.

Whole life

This is the traditional form of cash value life insurance. Also referred to as "ordinary life" or "straight life," whole life insurance provides coverage for your entire lifetime.

The premium depends on your age at the time you buy and stays the same as you grow older. The lowest premiums go to those who buy it when they are young, because they will pay into it the longest. Your cash value grows based on a fixed interest rate set each year in your policy by the company.

Some whole life policies let you pay premiums for a shorter time, such as 15 years, or until you reach age 65. Premiums for these policies are higher because you make premium payments during a short time frame.

Universal life

This is a type of flexible cash value policy that lets you vary your premium payments. You can also make limited adjustments in the death benefit amount of your policy. The company credits the premium you pay to a policy account that earns interest. The company then deducts the expense charges from the account. If your yearly premiums plus the interest the company credits to your account is greater than the cost of the insurance, your account will grow. However, if your premiums and interest earnings are less than the cost of insurance, your account will decrease. If your account keeps dropping, your coverage will end. To prevent this, you can increase your premium payments or lower the death benefits.

Variable life

As with universal life, the death benefit and cash values of variable life insurance vary. With variable life, the company invests your cash values into separate investment accounts, such as portfolios of stocks, bonds, and other investments. These separate accounts are like mutual funds. The company should provide you with information (also called a prospectus) that describes each separate account. Study the information carefully. As the policy owner, you choose the separate account to invest the cash value. The cash values and death benefit vary due to increases or decreases in the value of the separate accounts. You take the investment risk as the policyholder in return for possible improved benefits.

Life insurance illustrations

For most individual policies, cash values, death benefits, or premiums vary based on factors the company cannot guarantee (such as interest rates). Companies use computer-generated illustrations, such as a table to show how policies perform over the years under given assumptions. The illustrations show how benefits that are not guaranteed will change each year as interest rates and other factors change. The illustrations also show what the company actually guarantees and what could happen in the future. Remember, no one knows what will happen in the future. If the policy does not perform well, be prepared to adjust your financial plans.

You should be aware that due to past sales abuse, companies cannot use the term "vanishing premium" in life insurance illustrations. Vanishing premiums imply that you start out making large premium payments for the first several years of your policy with the possibility of no payments later on. There is NO guarantee this will occur.

Other life insurance policy options

The following are other popular types of life insurance:

Group life insurance

Typically purchased one year at a time, group life insurance gives you very little control over the conditions of the coverage. You buy group life through an association of individuals. For example, an association of individuals affiliated with an employer, labor union or credit union. In Washington state, if you leave a group life plan or your employer drops the plan, the law requires group life insurance to allow you to convert to permanent whole life insurance coverage.

The advantages to group life include:

- Group life insurance may cost less than individually purchased life policies
- Employers may choose to subsidize part of the cost as a fringe benefit for their employees
- It usually doesn't require a medical exam or health history

The disadvantages to group life include:

- It does not typically guarantee premiums
- It does not typically guarantee a renewable policy
- Group life coverage only applies to members of the group
- If you leave the group or drop your association membership, your coverage ends — unless you convert the policy to private insurance at a higher cost

Convertible policies

This type of policy starts out as term life insurance and then converts to a cash value life insurance policy. Young people who want financial security for their new families, but cannot afford cash value life insurance, may choose a convertible term insurance policy. These policies give you the option to convert your coverage to cash value life insurance for a limited time—without providing health information and some other proof of insurability and at the insurer's current premium rates. Premium rates start fairly low and then rise after you convert. When you shop for term insurance, look for policies that are both renewable and convertible.

Joint life insurance

When a husband and wife or business associates need life insurance, it is often cheaper to buy a joint life insurance policy instead of two or more separate policies. While this type of insurance saves on administrative costs, the policy usually only pays the death benefit on the first to die. However, some companies issue "second or last to die" policies for estate planning.

Family insurance

This is basically a whole life insurance policy on a parent with smaller amounts of additional term insurance on other family members.

Final expense insurance

Also known as "burial policies" or "senior life insurance packages," these small policies cover or pre-pay a person's funeral costs. Historically, some of these policies had a very high price compared to the death benefit. In response to consumer complaints, Washington created the high-priced life insurance regulation.

This regulation includes a special formula that bans companies from marketing certain high-priced life insurance policies with small death benefits. Companies cannot sell life insurance polices in Washington when the amount paid into them quickly exceeds the possible benefit. For example, during the first 10 years of the policy, the death benefit must be greater than the sum of the premiums compounded at five percent interest. Otherwise, you would be better off with your money in a savings account.

Please note: **This rule does not apply to policies with a death benefit of $25,000 or more.**

Optional policy benefits

Waiver of premium

If you become seriously ill or injured and cannot work, you may not be able to pay your premium. A waiver of premium benefit lets you waive paying your premiums as long as you remain disabled (according the definition in your policy). You must remain disabled at least six months to collect this modest disability income benefit. You can usually add this life insurance extra to your policy for only a few cents more per month per thousand dollars of insurance coverage.

Accidental death benefit

The industry also refers to this life insurance extra, as "double, triple, or additional" indemnity. If an accident causes your death, this life insurance extra allows your beneficiaries to receive double, triple, or even more of your policy's death benefit value.

Accelerated life insurance benefit

This permits life insurance companies to include policy language that allows for an early, discounted benefit payment to terminally ill policyholders. A doctor must certify that policyholders have less than 24 months to live.

What you should know about trading in policies

It's become more common for policyholders to use their life insurance cash values in various financial actions. Some people borrow the base value of their policy to take advantage of the low interest rate. Some cash their policies in and put the cash in higher interest accounts while making other plans for their insurance needs. Others may look into new developments in the life insurance market, such as policies that include investments or variable interest options.

Be careful if you are tempted to use your life insurance coverage as described in these examples. Your individual and family situation will help you decide if any of these options will work for you.

If you decide to change your coverage, you should never drop your old policy until the new one takes effect, and you have reviewed it. Ask your agent or broker for complete disclosure on any new policy you are thinking about buying.

If an agent or broker suggests you exchange a policy for a new one, ask for a comparison of the new offering and the old policy. Be sure to get it in writing before you agree to the transaction.

Be aware that any replacement policy may contain new restrictions such as a new two-year suicide clause, and may allow the company to revoke your policy for false statements on your application. Replacement policies may also include important new surrender penalties if you wish to cash them in. A surrender penalty is a financial penalty you pay for canceling a policy or contract early. Older people should be wary of trading in current policies for new ones that require a substantial new surrender penalty.

If you trade in policies, by law you must receive a "Notice Regarding Replacement of Insurance." This will help you make the best decision when you're thinking about replacing an existing life insurance policy. The agent or broker should give you a completed replacement notice at the time he or she takes your applications for the new insurance policy.

The "free-look" rule also applies to consumers who exchange one policy for another. (For an explanation of the free-look rule, see page 2).

What you should know about death claims

The company's home office usually handles life insurance claims. Your beneficiary will need to notify the company and request a claim form. Your beneficiary should expect to provide the company's claim department with:

- A completed claim form
- A certified copy of the death certificate
- The life insurance policy or a lost policy affidavit

Your beneficiary should keep copies of the documents he or she sends to the company.

Typically, beneficiaries will get a death-claim settlement from the company once he or she provides due proof of the policyholder's death, and turns in the policy. Due proof is what the company normally requires to establish that death occurred. Your beneficiary can provide due proof with one of the following:

- Death certificate from the Office of Vital Statistics
- Coroner's report
- Attending doctor's statement
- Hospital certificate of death

Individual policies

To ensure prompt settlements, insurers must pay your beneficiary no less than 8 percent interest starting from the date of death. An additional 3 percent is payable on those claims not settled within 90 days of when the beneficiary provided proof of death.

What your beneficiary can expect

In most instances, your beneficiary will receive the death benefit amount of the policy. Although, the insurer may adjust the amount depending on the specifics of your coverage. For example, any loan against the cash value of the policy and any interest due on such a loan may reduce the face amount. Also, adding any premium payments made in advance, or subtracting premiums due may adjust the face value. For a dividend paying policy, the insurer adds accrued dividends to the death benefit amount of the policy.

Settlement options

Beneficiaries normally have several options. They may choose to:

- Receive the policy proceeds in cash as soon as the claim is settled
- Leave the proceeds with the company, while it earns interest, until they decide what to do
- Convert the proceeds into monthly income

For example, companies usually offer beneficiaries several options to receive payment. One method draws the amount down in equal monthly payments over a fixed time, such as 10 years. Another method places the proceeds in a life annuity, which will pay a monthly amount for as long as your beneficiary lives. Yet another method provides a joint annuity—one that pays as long as your two beneficiaries live.

Your policy must include a section explaining these settlement options.

Options for seriously ill people

Viaticals

Many individuals who suffer serious, terminal illnesses realize one of their most valuable assets is a life insurance policy. However, only the beneficiary has access to this asset after the policyholder passes away. Viaticals give the policyholder access to this asset prior to his or her death. Viatical companies arrange the "sale" of life insurance benefits as an investment. Typically, an investor agrees to buy the life insurance policy of a seriously ill person by paying the person an amount less than the benefit. The seriously ill person receives much needed cash, and the buyer receives the full amount of the benefit. This benefit is payable once the former policyholder dies.

Other options

If you own a cash value policy, you could take a loan from the policy to help pay expenses. Also, if your policy contains an accelerated benefits option for catastrophic illness, you may qualify for a discounted payment from the face amount of the policy.

Commissioner Kreidler's Top 10 Life Insurance Cautions

1. Beware if it sounds too good to be true. It probably is NOT true.

2. Never sign a form that leaves blank spaces—even if the agent or broker assures you it is merely a formality.

3. If someone offers you a chance to turn in a small policy for a larger one without paying substantially more, WATCH OUT!

4. Don't drop your old policy until your new policy takes effect.

5. Save every piece of paper explaining your coverage and your policy. Keep them on file with your policy. (If the agent used a laptop computer, insist on a hard copy version of what he or she showed you.)

6. Never buy coverage you don't understand. It is the responsibility of the agent, broker or company to explain your coverage in terms you can understand.

7. Don't let someone pressure you. You do NOT face any deadlines.

8. Don't buy life insurance portrayed as a "pension plan" or a "retirement fund." Life insurance is NOT a pension plan.

9. Be careful of any life insurance plan that promises "vanishing premiums" or guarantees you a premium-free policy over a specific period.

10. Never ignore notices from the insurance company even though your agent tells you it's a "mistake" and nothing to worry about.

Need more help?

Call our Insurance Consumer Hotline!

1-800-562-6900

Our professional consumer advocates enforce insurance law and can investigate complaints against insurance companies and agents on your behalf.

We also offer individual counseling and group education on health care issues in your communities. Our highly trained Statewide Health Insurance Benefits Advisors (SHIBA) HelpLine volunteers can help you understand your rights and options regarding health care coverage, prescription drugs, government programs, and more.

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